Robert A. Sacks (SBN 150146)
(sacksr@sullcrom.com)
SULLIVAN & CROMWELL LLP
1888 Century Park East
Los Angeles, California 90067
Telephone: (310) 712-6600
Facsimile: (310) 712-8800

Brendan P. Cullen (SBN 194057)
(cullenb@sullcrom.com)
Scott C. Hall (SBN 232492)
(halls@sullcrom.com)
Sverker K. Hogberg (SBN 244640)
(hogbergs@sullcrom.com)
Achyut J. Phadke (SBN 261567)
(phadkea@sullcrom.com)
SULLIVAN & CROMWELL LLP
1870 Embarcadero Road
Palo Alto, California 94303
Telephone: (650) 461-5600
Facsimile: (650) 461-5700

Attorneys for Defendants VERIFONE HOLDINGS, INC., DOUGLAS G. BERGERON, WILLIAM G. ATKINSON and CRAIG A. BONDY

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

IN RE VERIFONE HOLDINGS, INC. SECURITIES LITIGATION	Master File No. C 07-6140 MHP
This Document Relates To: All Actions	**CLASS ACTION**
	DEFENDANTS' NOTICE OF MOTION AND MOTION TO DISMISS THE SECOND AMENDED CONSOLIDATED CLASS ACTION COMPLAINT; MEMORANDUM OF LAW IN SUPPORT THEREOF
	Judge: The Hon. Marilyn H. Patel Courtroom 15 Hearing Date: May 17, 2010 Hearing Time: 2:00 p.m.

NOTICE OF MOTION AND MOTION

TO PLAINTIFF AND ITS ATTORNEYS OF RECORD:

PLEASE TAKE NOTICE that on May 17, 2010 at 2:00 p.m., or as soon thereafter as counsel may be heard in Courtroom 15 of the United States District Court for the Northern District of California, located at 450 Golden Gate Avenue, San Francisco, California 94102, Defendants VeriFone Holdings Inc., Douglas Bergeron, William Atkinson and Craig Bondy will and hereby do move this Court to dismiss the Second Amended Consolidated Complaint and related documents on the ground that it fails to state a claim upon which relief can be granted. This Motion is made pursuant to the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), 15 U.S.C. § 78u-4(a) *et seq.*, and Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure, and is based on this Notice of Motion, the accompanying Memorandum of Points and Authorities, the motions and Memoranda of Points and Authorities respectively filed by defendants Barry Zwarenstein and Paul Periolat, all pleadings and papers filed herein, oral argument of counsel, and any matter which may be submitted at the hearing.

Date: March 5, 2010

/s/ Brendan P. Cullen

Brendan P. Cullen (SBN 194057)
Scott C. Hall (SBN 232492)
Sverker K. Hogberg (SBN 244640)
Achyut J. Phadke (SBN 261567)
SULLIVAN & CROMWELL LLP
1870 Embarcadero Road
Palo Alto, California 94303
Telephone: (650) 461-5600
Facsimile: (650) 461-5700

Robert A. Sacks (SBN 150146)
SULLIVAN & CROMWELL LLP
1888 Century Park East
Los Angeles, California 90067
Telephone: (310) 712-6600
Facsimile: (310) 712-8800

Attorneys for Defendants VERIFONE HOLDINGS, INC., DOUGLAS G. BERGERON, WILLIAM G. ATKINSON and CRAIG A. BONDY

TABLE OF CONTENTS

Page

PRELIMINARY STATEMENT 1
STATEMENT OF FACTS AND ALLEGATIONS 2
Background 2
Dismissal of Plaintiff's Consolidated Complaint 2
Allegations of the Second Amended Complaint 4
ARGUMENT 5
I. Plaintiff Again Fails to Plead Scienter Adequately 5
A. The PSLRA Establishes Exacting Standards for Pleading Scienter 5
B. The New Allegations of the SAC Do Not Raise a Strong Inference of Scienter 6
1. The SEC Complaint Does Not Raise a Strong Inference of Scienter 6
a. The SEC Complaint Provides a Cogent Explanation of Accounting Mistakes that Undermines an Inference of Scienter 8
b. The SEC Complaint Does Not Support an Inference of Scienter 10
2. The Three New Confidential Witnesses Do Not Raise a Strong Inference of Scienter 12
a. CW11 and CW12 12
b. CW13 14
3. Even if Periolat's Scienter Were Adequately Pleaded, This Is Not Attributable to Any Other Defendant. 15
C. Plaintiff Has Failed to Cure the Deficiencies of the Consolidated Complaint 16
1. Defendants' Stock Trades Still Do Not Raise a Strong Inference of Scienter 16
a. The Amount of Defendants' Stock Trades Was Not Unusual 17
b. The Timing of Sales and Trading History Were Not Unusual 19
2. VeriFone's Restatement Still Does Not Raise a Strong Inference of Scienter 20
3. Plaintiff's Other Recycled Allegations Still Do Not Raise a Strong Inference of Scienter 22
D. The Totality of Plaintiff's Allegations Do Not Raise a Strong Inference of Scienter 23
II. Plaintiff Fails to State a Claim Under Section 10(b) and SEC Rule 10b-5 or Under Section 20A for Insider Trading Against Defendants 23
III. Plaintiff Fails to State a Claim Under Section 20(a) for Control Person Liability Against Any Defendant 24
IV. The Second Amended Complaint Should Be Dismissed With Prejudice 25

TABLE OF AUTHORITIES

Page(s)

FEDERAL CASES

Berson v. *Applied Signal Tech., Inc.*
527 F.3d 982 (9th Cir. 2008) 21

Brodsky v. *Yahoo! Inc.*
630 F. Supp. 2d 1104 (N.D. Cal. 2009) 18

Cozarelli v. *Inspire Pharmaceuticals Inc.*
549 F.3d 618 (4th Cir. 2008) 6

Dent v. *U.S. Tennis Ass'n*
No. CV-08-1533, 2008 WL 2483288 (E.D.N.Y. June 17, 2008) 7

Dura Pharmaceuticals, Inc. v. *Broudo*
544 U.S. 336 (2005) 5

Glazer Capital Management v. *Magistri*
549 F.3d 736 (9th Cir. 2008) 6, 16

Higginbotham v. *Baxter Int'l, Inc.*
495 F.3d 753 (7th Cir. 2007) 12

In re Apple Computer, Inc., Sec. Litig.
243 F. Supp. 2d 1012 (N.D. Cal. 2002) 15

In re ASTResearch Sec. Litig.
887 F. Supp. 231 (C.D. Cal. 1995) 24

In re Cadence Design Sys., Inc., Sec. Litig.
654 F. Supp. 2d 1037 (N.D. Cal. 2009) 21

In re Countrywide Fin. Corp. Sec. Litig.
588 F. Supp. 2d 1132 (C.D. Cal. 2008) 24

In re Hansen Natural Corp. Sec. Litig.
527 F. Supp. 2d 1142 (C.D. Cal. 2007) 25

In re Int'l Rectifier Corp. Sec. Litig.
No. CV 07-2544-JFW, 2008 WL 4555794 (C.D. Cal. May 23, 2008) 15

In re McKesson HBOC, Inc. Sec. Litig.
126 F. Supp. 2d 1248 (N.D. Cal. 2000) 24

In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig.
218 F.R.D. 76 (S.D.N.Y. 2003) 7

In re Silicon Graphics Inc. Sec. Litig.
183 F.3d 970 (9th Cir. 1999) 6

In re Vantive Corp. Sec. Litig.
283 F.3d 1079 (9th Cir. 2002) ..... *passim*

In re Worlds of Wonder Sec. Litig.
35 F.3d 1407 (9th Cir. 1994) 17

Ind. Elec. Workers' Pension Trust Fund IBEW v. *Shaw Group, Inc.*
537 F.3d 527 (5th Cir. 2008) 12

Lipsky v. *Commonwealth United Corp.*
551 F.2d 887 (2d Cir. 1976).....7

Lipton v. *Pathogenesis Corp.*
284 F.3d 1027 (9th Cir. 2002) 23

Metzler Inv. GMBH v. *Corinthian Colleges, Inc.*
540 F.3d 1049 (9th Cir. 2008) 5, 16, 18, 19

Neubronner v. *Milken*
6 F.3d 666 (9th Cir. 1993) 24

Nordstrom v. *Chubb*
54 F.3d 1424 (9th Cir. 1995) 16

RSM Prod. Corp. v. *Fridman*
643 F. Supp. 2d 382 (S.D.N.Y. 2009).....7

Sanders v. *Brown*
504 F.3d 903 (9th Cir. 2007) 5

Tellabs, Inc. v. *Makor Issues & Rights, Ltd.*
551 U.S. 308 (2007).....2, 6, 12

Zucco Partners, LLC v. *Digimarc Corp.*
552 F.3d 981 (9th Cir. 2009) ..... *passim*

FEDERAL STATUTES

Fed. R. Civ. P. 9(b) 5

Fed. R. Civ. P. 12(b)(6).....5

Fed. R. Civ. P. 12(f).....7

15 U.S.C. § 78b.....6
15 U.S.C. § 78j(b) [Section 10(b)]..... *passim*
15 U.S.C. § 78t-1(a) [Section 20A] 2, 4, 23, 24
15 U.S.C. § 78t(a) [Section 20(a)] 2, 4, 24
15 U.S.C. § 78u-4(a) *et seq.* [PSLRA]..... *passim*
17 C.F.R. § 240.10b5-1 [SEC Rule 10b-5].....5, 23, 24

MEMORANDUM OF POINTS AND AUTHORITIES

Defendants VeriFone Holdings, Inc. ("VeriFone" or the "Company"), Douglas Bergeron, William Atkinson, and Craig Bondy (collectively, "Defendants") submit this Memorandum in support of their motion to dismiss the Second Amended Consolidated Complaint ("Second Amended Complaint" or "SAC"), filed by Lead Plaintiff National Elevator Industry Pension Fund ("Plaintiff"). Defendants hereby incorporate by reference the arguments and authorities contained in the Memoranda of Points and Authorities respectively submitted on behalf of defendants Barry Zwarenstein and Paul Periolat.

PRELIMINARY STATEMENT

Ignoring this Court's order that the amended complaint be "more in the form of a 'short and plain statement,'" (Memorandum & Order of May 26, 2009, Docket Entry ("D.E.") 191 ("Order"), at 16), Plaintiff returns with a 98-page behemoth.[1] But like the equally prolix Consolidated Complaint ("CC") that this Court dismissed, the SAC fails to plead scienter on the part of any Defendant. The bulk of the SAC consists of the same allegations that this Court found wanting in the prior complaint. Even where this Court provided Plaintiff a road map to improve its allegations – with respect to Defendants' stock sales – Plaintiff's allegations are still as inadequate and for the same reasons as last time.

Plaintiff's new allegations not only fail to give rise to the required strong inference of scienter, they actually tend to suggest the opposite – that the mistakes disclosed in the restatement were just that: mistakes. Plaintiff makes extensive use – or misuse – of the Securities and Exchange Commission's civil complaint in *Sec. & Exch. Comm'n* v. *VeriFone Holdings, Inc.* (the "SEC Complaint"). The extent to which the SEC Complaint undermines Plaintiff's case is evidenced by the lengths to which Plaintiff goes to characterize the SEC Complaint as something it manifestly is not. The allegations of the SEC Complaint are, of course, just allegations and for that reason alone are of limited usefulness to Plaintiff. But, worse for Plaintiff, they are allegations not of fraud or of intentional wrongdoing. The SEC did not charge VeriFone or any officer or director with any intentional wrongdoing. Its complaint describes a series of mistakes – and it describes them the way one would describe mistakes. Notwithstanding Plaintiff's misleading quotations from it, the SEC Complaint, filed

[1] The 98-page SAC itself amends the 96-page First Amended Complaint (D.E. 205) by adding Paul Periolat as a defendant.

after the SEC conducted an investigation into the causes of VeriFone's restatement, supports just the opposite of a strong inference of scienter on the part of any Defendant.

Plaintiff's remaining new allegations are from three more confidential witnesses ("CWs") (the same ten CWs from the prior complaint reprise their roles, rehearsing the same scienter-free assertions, in the SAC). The new CWs fare no better, failing to allege that they or anyone else engaged in fraud or intentional misconduct of any kind. These new CWs do not even purport ever to have communicated with Defendants Bergeron or Zwarenstein, and nothing in the CWs' allegations remotely provides competent evidence of any mental state on the part of Bergeron or Zwarenstein.

Taken individually or together, the allegations of the SAC are just as insufficient to raise the required "cogent" and "compelling" inference of scienter as those in Plaintiff's last complaint. *See Tellabs, Inc.* v. *Makor Issues & Rights, Ltd.*, 551 U.S. 308, 324 (2007).

Plaintiff's insider trading claims under Sections 10(b) and 20A warrant dismissal again because Plaintiff fails to plead scienter adequately, and because Plaintiff does not allege adequately that Defendants possessed material non-public information or engaged in contemporaneous trading. Plaintiff's claims under Section 20(a) for "control person" liability also fail once more, as Plaintiff has not pleaded a requisite primary violation or adequately alleged "control" on the part of any Defendant.

The SAC should be dismissed with prejudice.

STATEMENT OF FACTS AND ALLEGATIONS

BACKGROUND

VeriFone designs, manufactures and markets secured electronic payment solutions for use by consumers and merchants. (Order at 1-2.) In November 2006, VeriFone acquired Israel-based Lipman Electronic Engineering Ltd. ("Lipman") and began work to integrate the two companies. (*Id.* at 2.) On December 3, 2007, VeriFone announced that it would restate its financial statements for the first three quarters of fiscal year 2007 due to accounting errors that caused VeriFone to overstate inventory and, thus, its gross margins and earnings. (*Id.*) Lawsuits were filed against Defendants the next day. (*Id.*) Ultimately, nine putative class actions were consolidated with Plaintiff as lead plaintiff. (*Id.* at 6.)

DISMISSAL OF PLAINTIFF'S CONSOLIDATED COMPLAINT

On May 26, 2009, this Court granted VeriFone's motion to dismiss Plaintiff's

Consolidated Complaint, holding that Plaintiff failed to allege scienter as required by the Private Securities Litigation Reform Act of 1995 ("PSLRA"). (*Id.* at 15-17.)

This Court determined that Plaintiff's allegations concerning Defendants' stock trades did not provide the basis for an inference of scienter because Plaintiff failed to base its allegations on a history of trades over a period of years with specific trade dates for each Defendant. (*Id.* at 9-10.) Even the data that Plaintiff belatedly provided in its opposition brief were described as "inadequate to meet the requirement of providing a 'meaningful trading history for purposes of comparison.'" (*Id.* at 10 (quoting *Zucco Partners, LLC* v. *Digimarc Corp.*, 552 F.3d 981, 1005 (9th Cir. 2009)).

Likewise, Plaintiff "pled nothing" to suggest that VeriFone's restatement, itself, evidenced scienter. (Order at 12.) The inventory accounting errors that led to the restatement "d[id] not have such prominence that it would be 'absurd' to suggest management had no knowledge of the matter," nor were the errors "obvious from the operations of the company" such that they "appear to be something about which [D]efendants 'must have known.'" (*Id.* at 11-12.) The Court thus held that "[g]enerally, the restatement of financials is not itself a ground to infer scienter." (*Id.* at 12.)

The other facts that Plaintiff alleged also fell short of showing scienter. Defendants' signatures on Sarbanes-Oxley certifications and their positions at the company "add[ed] nothing substantial to the scienter inquiry." (*Id.* at 13.) The Court found that Plaintiff's allegations based on CWs, who described the disorganization of VeriFone's accounting department after its merger with Lipman, merely indicated that VeriFone was "overwhelmed or underprepared to confront the challenges before it," and "d[id] not raise an inference of scienter." (*Id.* at 13.) Plaintiff alleged "no facts . . . to support [its] interpretation" that personnel changes involving Defendants were evidence of scienter. (*Id.* at 14.) Defendants' forward-looking statements from 2006 gave no support to Plaintiff's allegations of scienter. (*Id.*) Plaintiff's reliance on revised projections made in 2008 to accompany the corrective restatement "ma[de] even less sense." (*Id.* at 14-15.) And, finally, Plaintiff's attempt to allege that Defendants' compensation was evidence of scienter failed because there was "no strong correlation" between financial results and compensation. (*Id.* at 15.)

The Court further held that Plaintiff's allegations of scienter "fare no better when read in combination than when read independently." (*Id.*) Accordingly, the Court dismissed Plaintiff's claim

under Section 10(b) of the Exchange Act. (*Id.*) As Plaintiff failed to state a Section 10(b) claim, the Court also dismissed Plaintiff's insider trading and control person claims under Section 20A and Section 20(a). (*Id.*) The Court granted Plaintiff leave to amend, observing that this was the first consolidated complaint and that "detailed and comprehensive comparisons of trades stretching over the course of a number of years . . . and containing specific dates for all sales may be more persuasive" if "activity during the class period was 'dramatically out of line with prior trading practices.'" (*Id.* at 16.)

ALLEGATIONS OF THE SECOND AMENDED COMPLAINT

The SAC sets forth many of the same factual allegations in support of scienter as did the Consolidated Complaint (D.E. 161). Once again, Plaintiff relies on Defendants' stock trades and on the fact of the restatement, itself, to support allegations of scienter, even though this Court rejected those very same attempts the first time. (*Compare* SAC ¶¶ 114, 116-25 *with* CC ¶¶ 77-78, 81-89; *and compare* SAC ¶¶ 199-215 *with* CC ¶¶ 136-44; *see also* Order at 9-10.) Yet again, the allegations of ten CWs regarding disorganization in VeriFone's accounting department after the Lipman merger are said to evidence scienter. (*Compare* SAC ¶¶ 157-70, 172-83 *with* CC ¶¶ 91-104, 106-17.) And once more, Plaintiff holds out as evidence of scienter Defendants' roles in the company and sworn public certifications (*compare* SAC ¶¶ 153, 155, 189 *with* CC ¶¶ 99, 126, 153, 181-84), specific personnel changes at VeriFone (*compare* SAC ¶¶ 185 *with* CC ¶¶ 119-20), forward-looking statements from 2006 (*compare* SAC ¶¶ 191-196 *with* CC ¶¶ 157-61), Defendants' incentive compensation (*compare* SAC ¶¶ 216-28 *with* CC ¶¶ 145-56), and details regarding Lipman's international sales and gross margins (*compare* SAC ¶¶ 146-52 *with* Pl.'s Opposition to Defs' Motions To Dismiss, D.E. 174 ("Pl.'s Opp."), at 13-14 and CC ¶¶ 54, 65-67, 73, 77, 133-34).

The new allegations are principally those allegations that Plaintiff purports to find in the SEC Complaint against VeriFone and its former supply chain controller, Paul Periolat. As described below, the allegations that Plaintiff attributes to the SEC and those that actually appear in the SEC Complaint bear little resemblance. Plaintiff misleadingly strings together – and then repeats and repeats – snippets from the SEC Complaint to insinuate that Defendants intentionally falsified VeriFone's financial statements. (*See* SAC ¶¶ 99-113.) As described below (*infra* § I.B.1.), however, the SEC made no factual allegation suggesting any knowledge or deliberate recklessness by Defendants Bergeron

or Zwarenstein with respect to Periolat's errors (or, for that matter, knowledge by Periolat that his inventory calculations were in error). (*See* SEC Compl. ¶¶ 11-32.)

Plaintiff's other new allegations relate to purported problems with inventory records and valuation and come from three new CWs. (SAC ¶¶ 128-37.) Plaintiff alleges, based on the claims of CW11 and CW12, that the inventory recordkeeping system at VeriFone's Lincoln, California facility was extremely disorganized after the VeriFone-Lipman merger, and that this disorganization is evidence of scienter. (*Id.* ¶¶ 59-60, 128-36; *see also id.* ¶¶ 157-70; CC ¶¶ 90-104.) Plaintiff also suggests that Defendants' public statements as to inventory values and controls were fraudulent in light of these inventory issues. (SAC ¶¶ 140-45.) Finally, Plaintiff points to the testimony of a third new CW, CW13, who claims to have submitted an analysis to VeriFone's supply chain finance group that suggested that inventory and overhead valuations were inflated and had this analysis rejected. (*Id.* ¶¶ 61, 137.)

ARGUMENT

"A motion to dismiss under Federal Rule of Civil Procedure 12(b)(6) 'tests the legal sufficiency of a claim.'" (Order at 7 (citation omitted).) Well-pleaded factual allegations are taken as true and construed in the light most favorable to the plaintiff. *Zucco Partners, LLC* v. *Digimarc Corp.*, 552 F.3d 981, 989 (9th Cir. 2009). "Conclusory allegations and unreasonable inferences, however, are insufficient to defeat a motion to dismiss." *Sanders* v. *Brown*, 504 F.3d 903, 910 (9th Cir. 2007). "[R]eview is generally limited to the face of the complaint, materials incorporated into the complaint by reference, and matters of which [the court] may take judicial notice." *Digimarc*, 552 F.3d at 989.

I. PLAINTIFF AGAIN FAILS TO PLEAD SCIENTER ADEQUATELY

The elements of a claim under Section 10(b) and Rule 10b-5 are: (1) a material representation or omission; (2) scienter, *i.e.*, a wrongful state of mind; (3) a connection with the purchase or sale of a security; (4) reliance; (5) economic loss; and (6) loss causation. *Dura Pharmaceuticals, Inc.* v. *Broudo*, 544 U.S. 336, 341-42 (2005).

A. The PSLRA Establishes Exacting Standards for Pleading Scienter

"[P]laintiffs in private securities fraud class actions face formidable pleading requirements to properly state a claim and avoid dismissal under Fed. R. Civ. P. 12(b)(6)." *Metzler Inv. GMBH* v. *Corinthian Colleges, Inc.*, 540 F.3d 1049, 1054-55 (9th Cir. 2008). Under Fed. R. Civ. P.

9(b), plaintiffs must plead fraud with particularity, a "requirement [that] has long been applied to securities fraud complaints." *Digimarc*, 552 F.3d at 990. The PSLRA imposes the additional requirement that a complaint "plead with particularity both falsity and scienter" and that sufficient facts be pleaded to establish a "strong inference" of scienter. *Id.* at 990-91 (internal citations omitted).

Under the "strong inference" standard, a "complaint will survive . . . only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged." *Tellabs*, 551 U.S. at 324. Mere allegations of recklessness will not suffice: "'[A]lthough facts showing mere recklessness or a motive to commit fraud and opportunity to do so may provide some reasonable inference of intent, they are not sufficient to establish a *strong* inference of deliberate recklessness.'" *Digimarc*, 552 F.3d at 991 (quoting *In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d 970, 974 (9th Cir. 1999) (emphasis in original)); (Order at 9).

B. The New Allegations of the SAC Do Not Raise a Strong Inference of Scienter

1. The SEC Complaint Does Not Raise a Strong Inference of Scienter

It is difficult to imagine a turn of events less helpful to a securities fraud plaintiff than to have the SEC – the government agency created to "insure the maintenance of fair and honest markets" in securities, 15 U.S.C. § 78b – complete an investigation into the conduct underlying that plaintiff's case and conclude that mistakes were made but that no one committed fraud. This is the situation Plaintiff was presented with in September 2009 when the SEC completed its investigation and filed a complaint against VeriFone and Paul Periolat that asserted no fraud claims and no claims at all against any officer or director of VeriFone. Plaintiff's attempt to make lemonade out of this lemon has chutzpah and a certain amount of ingenuity going for it, but not much else.

In the first place, the fact that the SEC has filed an action against a company is not evidence of scienter – *even if that action asserts intentional wrongdoing by the company*. *See Glazer Capital Management* v. *Magistri*, 549 F.3d 736, 748-49 (9th Cir. 2008) (holding that allegations based on DOJ and SEC settlement agreement did not plead scienter under PSLRA).[2] The allegations of the

[2] Nor does the fact that there was an SEC investigation support an inference of scienter. *See, e.g.*, *Cozarelli* v. *Inspire Pharmaceuticals Inc.*, 549 F.3d 618, 628 n.2 (4th Cir. 2008) (noting that allegation of SEC investigation in private securities complaint does not "add much, if anything, to an

SEC Complaint are just that – allegations. Allegations lifted from a separate complaint do not equate to well-pleaded, particularized facts. As numerous courts have held, "references to preliminary steps in litigations and administrative proceedings that did not result in an adjudication on the merits or legal or permissible findings of fact are, as a matter of law, immaterial under Rule 12(f) of the Federal Rules of Civil Procedure." *In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig.*, 218 F.R.D. 76, 78-79 (S.D.N.Y. 2003) (striking private securities complaint's references and adoption of allegations of SEC and NASD complaints) (*citing Lipsky* v. *Commonwealth United Corp.*, 551 F.2d 887, 892-94 (2d Cir. 1976)). This includes "paragraphs in a complaint that are either based on, or rely on, complaints in other actions that have been dismissed, settled, or otherwise not resolved." *RSM Prod. Corp.* v. *Fridman*, 643 F. Supp. 2d 382, 403 (S.D.N.Y. 2009) (striking references to "complaints filed in actions that were never resolved on the merits" because they are immaterial as a matter of law). In VeriFone's case, the SEC Complaint was settled *without* adjudication on the merits and *without* any admission by VeriFone to the allegations contained therein. (*See* Final Judgments against VeriFone and Periolat, attached as Exs. A and B, respectively, to the Declaration of Brendan P. Cullen ("Cullen Decl.").)

Thus, even if Plaintiff had fairly quoted the SEC's allegations (and even if those allegations were *proved*), they would fail to provide factual support for an inference of scienter.[3] *See generally Dent* v. *U.S. Tennis Ass'n*, No. CV-08-1533, 2008 WL 2483288, at *3 (E.D.N.Y. June 17, 2008) ("In addition to being inadmissible as hearsay, unproved allegations of misconduct are not proof of anything."). But here, where the SEC Complaint's allegations are flatly inconsistent with the notion that anyone engaged in intentional misconduct, the call is not a close one.

---

inference of scienter," where parties indicated that "the SEC's investigation has already settled without a finding of culpability for securities fraud.").

[3] If allegations taken from another complaint cannot help Plaintiff meet its pleading burden, then statements from a press release purporting to describe a complaint obviously cannot either. Plaintiff undoubtedly understands this, which may explain its practice of quoting phrases from the SEC's press release that accompanied the filing of the SEC Complaint as though they were part of the SEC Complaint. So, for example, when Plaintiff alleges that "Bergeron and Zwarenstein . . . instructed Periolat and other financial personnel to . . . '***fix the problem***' so that defendants could '***report results in line with forecasts***,'" Plaintiff cites on to ¶ 17 of the SEC Complaint (*see* SAC ¶ 104). But the highlighted portion of that quote is nowhere to be found in the SEC Complaint – it appeared only in the press release. (*See* SEC Litigation Release of September 1, 2009, SAC, Ex. 1.)

a. The SEC Complaint Provides a Cogent Explanation of Accounting Mistakes that Undermines an Inference of Scienter

The allegations of the SEC Complaint describe the SEC's view of the circumstances that gave rise to VeriFone's December 3, 2007 restatement announcement. Not only are the circumstances described by the SEC devoid of indicia of fraud, they are described in a way that squarely conflicts with a fraud claim.[4] Because Plaintiff so fundamentally misdescribes the SEC Complaint, the actual allegations of that complaint bear a careful reading.

The SEC alleges that, in early February 2007, internal preliminary results at VeriFone for the first quarter of FY 2007 showed a gross margin approximately 4% lower than VeriFone (and Paul Periolat in particular) had forecasted. (SEC Compl. ¶ 14.) Periolat and others, the SEC alleges, "were charged with determining why there was such a large discrepancy" between the preliminary results and the forecasts. (*Id.* ¶ 15.) "In the past, Periolat's forecasts had been accurate and relied on by VeriFone senior management, so there was considerable concern" over the discrepancy. (*Id.*) Because gross margin increases with a reduction in cost of goods sold ("COGS"), "Periolat and others focused on COGS and inventory accounting to determine the reasons for the variance." (*Id.* ¶ 16.) VeriFone's CEO and then-CFO (by which the SEC presumably means to refer to Bergeron and Zwarenstein), are alleged to have "express[ed] increasing frustration" and "sent emails characterizing the low gross margin as an 'unmitigated disaster' and instructed management to 'figure it [and related low results] out.'" (*Id.* ¶ 17 (alteration in original).) "In addition, Periolat and others were provided with analyses which laid out the relation between specific reductions in COGS and the corresponding increase in gross margin." (*Id.*)

The SEC alleges that Periolat then erroneously determined that the problem was caused by incorrect accounting for inventory at certain of the former Lipman entities. (*Id.* ¶ 18.) He made a manual accounting adjustment of $7 million, as a result of which VeriFone's gross margin increased. (*Id.*) The SEC alleges that Periolat "failed to take adequate steps to verify that [the adjustment] was appropriate." (*Id.* ¶ 19.) In particular, he is alleged to have failed to confirm the adjustments with

[4] Lest Defendants again be accused of using the SEC Complaint as a "sword" (such that the "shield" of the PSLRA discovery stay should be lifted (D.E. 200; D.E. 222)), it bears emphasizing that Defendants are simply responding to those allegations that Plaintiff purportedly bases on the SEC Complaint and demonstrating that that complaint does not assist Plaintiff in pleading the required "strong inference" of scienter in this case.

Lipman's controller. (*Id.*) Had he done so, the SEC contends that he would have learned that Lipman's inventory report was correct and his manual adjustment was in error. (*Id.*) The SEC further alleges that Periolat was also aware that Lipman had proper procedures in place for accounting inventory, and that, one month after the close of the quarter, Periolat learned that Lipman had correctly accounted for inventory through fiscal year 2006, putting him on notice that his adjustments may have been incorrect. (*Id.* ¶ 20.) Periolat did not verify or correct his prior adjustment, the SEC alleges. (*Id.*)

The SEC contends that neither Periolat's supervisor nor any other senior manager reviewed his work, and VeriFone did not have procedures in place to prevent the person responsible for internal forecasting from later making adjustments to allow VeriFone to meet those forecasts. (*Id.* ¶ 21.) As a result, VeriFone overstated its net income by $12.4 million. (*Id.* ¶ 22.)

According to the SEC, at the end of the second and third quarters of FY 2007, VeriFone's internal preliminary results again reflected lower gross margins than VeriFone's forecasts and public guidance. (*Id.* ¶ 23.) At the end of both quarters, Periolat is alleged to have determined that the reason for the lower-than-expected gross margins was a failure to account for in-transit inventory (reflecting inventory shipped overseas from a VeriFone subsidiary but not yet received in the United States). (*Id.* ¶¶ 24-25.) For both quarters, the SEC alleges, Periolat incorrectly determined, based on shipping and receiving reports, that there was a gap between inventory shipped and inventory received. (*Id.*) Periolat purportedly received positive feedback from a subordinate and then entered his adjustments into VeriFone's financial reporting system. (*Id.*) The SEC concludes that "[t]here was no reasonable basis for the manual entries," which relied on an allegedly unfounded assumption that goods were in transit between overseas headquarters and the United States when no goods were actually shipped. (*Id.* ¶ 26.)

"[N]o one reviewed Periolat's work during the second and third quarters closing process," alleges the SEC. (*Id.* ¶ 27.) "Senior management was aware of his adjustments but never questioned them." (*Id.*) "Senior management" is also alleged not to have questioned the initial forecasts for the second and third quarters; "instead, they simply assumed the preliminary actual results were wrong when they differed from the forecasts." (*Id.*)

The SEC alleges that the "accounting irregularities came to light in late November 2007 during the annual audit. Periolat was unable to explain his adjustments and ultimately concluded that

they were wrong. He then reported the problem to senior management." (*Id*. ¶ 29.)

b. The SEC Complaint Does Not Support an Inference of Scienter

Given what the SEC Complaint actually alleges, Plaintiff's attempt to use this document to its advantage in pursuing a fraud case against Defendants is senseless. There is no support in the SEC Complaint for Plaintiff's allegation that Periolat knowingly created fictitious entries at Bergeron's and Zwarenstein's encouragement or direction. (*See* SAC ¶¶ 105-06 (alleging that "Periolat created fictitious inventory, which reduced COGS and falsified gross margin and earnings, just as he was encouraged to do"); *id.* ¶ 104 ("Bergeron and Zwarenstein . . . instructed Periolat and other financial personnel to . . . '*fix the problem*' so that defendants could '*report results in line with forecasts*'").) While the SEC Complaint alleges that "Periolat and others were charged with determining why there was such a large discrepancy" between preliminary results and the forecast, it does not allege that it was Bergeron or Zwarenstein who "charged" Periolat with this task or that they directed or encouraged any fraudulent accounting. (SEC Compl. ¶ 15.) There is no allegation in the SEC Complaint that Bergeron or Zwarenstein communicated with Periolat at all.[5] Rather, the SEC Complaint alleges that Bergeron and Zwarenstein "instructed *management*" – not Periolat – "to 'figure it [and related low results] out.'" (*Id*. ¶ 17 (emphasis added; bracketed material in original).) Periolat was allegedly "provided with analyses which laid out the relation between specific reductions in COGS and the corresponding increase in gross margin," but the SEC Complaint does not allege that Bergeron or Zwarenstein provided Periolat with these analyses, saw these analyses, or had any idea that Periolat had them, let alone encouraged Periolat to make inaccurate entries based on them. (*Id*. ¶ 17.) The SEC Complaint does not allege that Periolat, himself – let alone two senior officers that the SEC Complaint does not allege he ever spoke to – knew that his entries were "fictitious" or erroneous when made.

The SEC's description of Periolat's entries contradicts any such notion. When Periolat made his first incorrect adjustment, the SEC alleges that it was because he "determined that the problem

[5] On this point, the actual allegations of the SEC Complaint are also in obvious conflict with Plaintiff's counsel's baseless assertion to this Court in a recent hearing that the SEC Complaint showed that "[Bergeron and Zwarenstein] were in the room with Periolat. He came to them and said, you know, 'Our numbers are not what we told the market they are.'" (Transcript of February 1, 2010 Proceedings, Cullen Decl. Ex. C, at 5.)

with the gross margin had been caused by incorrect accounting for inventory by a foreign subsidiary," (*id*. ¶ 18), not because he was allegedly told to produce a particular number or result. His second incorrect entry was made, the SEC alleges, because "Periolat determined that the reason for the lower-than-expected gross margin was a failure to properly account for in-transit inventory," (*id*. ¶ 24), not, again, because he was told to ensure that VeriFone made a particular number. The allegation that Periolat "was unable to explain his adjustments and *ultimately concluded* that they were wrong," (*id*. ¶ 29 (emphasis added)), makes no sense in the context of a fraud complaint – if the SEC had actually accused Periolat of making false entries at the instance of VeriFone management, the SEC would not assert that Periolat "ultimately concluded" that his adjustments were wrong months after the adjustments were made. He would have known that from the moment he made them. Likewise, if the SEC intended to allege that "senior management" knew that the entries were incorrect from the beginning, then alleging that Periolat "reported the problem to senior management" in late November 2007, (*id*.), is a strange word choice since "senior management" would have been aware of the "problem" all along.

Plaintiff also alleges that, because the SEC alleged that "[s]enior management was aware of Periolat's adjustments but never questioned them," (*id.* ¶ 17), Bergeron and Zwarenstein therefore possessed scienter with respect to their statements during the first and second quarter conference calls. (SAC ¶¶ 108-10.) Even if "senior management" is to be understood as a reference to Bergeron and Zwarenstein (the term is nowhere defined in the SEC Complaint), the SEC Complaint does not allege – or even hint – that Bergeron or Zwarenstein or anyone else was aware that Periolat's accounting adjustments were incorrect. (SEC Compl. ¶ 27.) The SEC Complaint alleges more than once that no member of senior management reviewed Periolat's entries or underlying work, (*id.* ¶¶ 21, 27), meaning that no member of senior management had the opportunity to learn that Periolat's entries were incorrect. Indeed, the SEC Complaint makes clear that "senior management" believed that the accounting adjustments made were *correct* because they "assumed the preliminary actual results," which were adjusted by Periolat's entries, "were wrong when they differed from the forecasts" – forecasts that had been accurate in the past. (*Id.* ¶¶ 15, 27.)[6]

[6] Plaintiff makes much of the SEC's citation to emails that describe the gap between the forecast and apparent actual results as an "unmitigated disaster." (SAC ¶¶ 11, 104.) Obviously, a substantial and

Plaintiff also fails to allege scienter in connection with Defendants' third quarter conference call statements. Plaintiff's manipulation of the SEC Complaint is especially stark here. (*See* SAC ¶ 112 ("Bergeron and Zwarenstein 'were aware of [Periolat's] adjustments' and knew there 'was no reasonable basis for the manual entries' because the 'goods were never actually shipped'"); *see also id.* ¶ 19.) Quoting from separate paragraphs in the SEC Complaint, and out of order, Plaintiff asserts without support that Bergeron and Zwarenstein *knew* there was no reasonable basis for Periolat's entries. The SEC Complaint, however, makes no such assertion. Rather, the SEC alleges that Periolat "incorrectly determined" that an inventory gap justified the adjustment. (SEC Compl. ¶ 24.) "Senior management" is merely alleged to have been aware of the adjustments. (*Id.* ¶ 27.) The SEC does not allege that Periolat, let alone "senior management," knew that the adjustments were in error when made.

2. The Three New Confidential Witnesses Do Not Raise a Strong Inference of Scienter

In the SAC, Plaintiff adds allegations from three more confidential witnesses pertaining to VeriFone's inventory control and records. (*See* SAC ¶¶ 59-61, 128-135, 137.) As the Ninth Circuit noted in *Digimarc*, multiple courts of appeals have held that the Supreme Court's decision in *Tellabs* requires a "stricter standard for evaluating the sufficiency of securities fraud complaints relying on confidential witnesses." 552 F.3d at 995 n.2. Some courts have "discount[ed]" CW allegations because "[i]t is hard to see how information from anonymous sources could be deemed 'compelling' or how we could take account of plausible opposing inferences." *Higginbotham* v. *Baxter Int'l, Inc.*, 495 F.3d 753, 756-57 (7th Cir. 2007); *accord Ind. Elec. Workers' Pension Trust Fund IBEW* v. *Shaw Group, Inc.*, 537 F.3d 527, 535 (5th Cir. 2008). But even at full retail, none of CW11, CW12, or CW13 provides any more basis for a strong inference of scienter than did CW1 through CW10.

a. CW11 and CW12

Plaintiff relies on allegations by CW11 (an independent contractor who worked for VeriFone for six months, leaving in May 2007) and CW12 (a warehouse manager who worked at VeriFone for nine months, starting after the first of Periolat's alleged adjustments) regarding general

---

unexpected (and unexplained) discrepancy between forecasted and actual results is troubling, and an executive can say so without meaning to communicate "this discrepancy must be resolved by fraud."

problems in physical inventory control at VeriFone's Lincoln, California facility. (SAC ¶¶ 59-60, 129-35.) These alleged statements come nowhere near demonstrating scienter on the part of any Defendant. Neither CW11 nor CW12 ever claims to have met, communicated with, or worked with any Defendant – neither of them mentions any Defendant by name or title. CW11 alleges that he or she participated in conference calls with his or her supervisors (neither of whom is a Defendant and neither of whom is even alleged to have reported to a Defendant) and "at least three VeriFone vice presidents from corporate headquarters in San Jose." (*Id*. ¶ 134.) Neither CW11 nor CW12 names these vice presidents, let alone alleges whether any of them communicated anything concerning the inventory issues to anyone senior to them. Accordingly, even if CW11 and CW12 themselves knew something about the problems that resulted in the restatement or knew that VeriFone's financial statements were false in some respect, they provide no basis to conclude that this knowledge was shared with or by any Defendant.

Just as importantly, however, nothing CW11 or CW12 describes has any relationship to VeriFone's restatement. The inventory problems described by CW11 and CW12 (that "inventory recorded on the [Oracle] 10.7 system as being located at the Lincoln facility did not exist" (SAC ¶¶ 59-60)), are not even the inventory problems that Plaintiff alleges led to the restatement. (*See* SAC ¶¶ 13-14, 16-19 (alleging that Periolat incorrectly allocated overhead to former Lipman inventory and prepared false journal entries that increased "in-transit" inventory even though "goods were never actually shipped between the international headquarters and the United States and as a result could not have been 'in transit'").) Inventory in former Lipman facilities and allegedly fictitious "in-transit" inventory would, of course, not exist – or be recorded on the Oracle system as existing – at the Lincoln warehouse. So, whether inventory was well or badly controlled at the Lincoln facility, Plaintiff does not allege any way in which VeriFone's financial statements were false as a consequence.[7] Neither CW11 nor CW12 alleges knowing anything about VeriFone's financial statements or about any accounting entry made by

[7] Given the total lack of any relationship between the inventory control problems described by CW11 and CW12, it is risible for Plaintiff to allege that the "25%-31% inventory inaccuracy from December 2006 to March 2007" that it attributes to CW11 is "corroborated by VeriFone's restatement which revealed that VeriFone's total inventory was overstated by ***23.59%*** in 2Q07 and ***38.75%*** in 3Q07." (SAC ¶ 133 (emphasis in original).) These inventory overstatements – from the quarters ending two and five months after the period described by CW11 – are alleged to have related to Periolat's in-transit inventory accounting entries, (*id*. ¶¶ 16, 18, 109, 111), not to any inventory problem in the warehouse where CW11 briefly worked.

Periolat or anyone else. They do not even attempt to describe the mental state of any Defendant as to these things, let alone do so plausibly. Accordingly, even if true, the allegations attributed to CW11 and CW12 cannot possibly establish scienter on the part of any Defendant.

b. CW13

Plaintiff also relies on the allegations of CW13, purportedly a former VeriFone employee who left the company in February 2008. CW13 alleges that he or she was asked in the first quarter of 2007 to assess an inventory valuation variance between the supply chain operations and supply chain finance groups, and that he/she determined that the supply chain finance group's inventory valuations were overvalued. (*Id.* ¶¶ 61, 137.) CW13 claims to have provided a report to "supervisors, including Periolat," that documented this supposed variance, which was allegedly met with "an e-mail from Periolat or Keith Schaall rejecting CW13's report." (*Id.*) As with CW11 and CW12, however, CW13 does not allege that he provided his report to, or shared any concerns over this purported inventory issue or VeriFone's financial statements with, Defendants Bergeron or Zwarenstein.

But even if he had communicated his inventory issue to Bergeron or Zwarenstein, that would not establish scienter. In the first place, it is not at all clear what inventory issue CW13 is describing or whether it has any relationship to the restatement – all available evidence strongly suggests that it does not. CW13's analysis is described as having occurred as to a variance that existed "in 1Q07." (*Id.*) That analysis purported to find that "improper in-transit accruals" had been applied to inventory in the *first* quarter of 2007. (*Id.* ¶ 61.) But the accounting errors that Plaintiff alleges gave rise to the restatement were not made until *after* the first quarter of 2007. (*Id.* ¶ 13 (errors "***after*** 1Q07 already closed . . . ." (emphasis in original); *id.* ¶¶ 16-19.) And the in-transit inventory errors were not alleged to have been made until after the second and third quarters. (*Id.* ¶¶ 16, 18, 119-20 (no mention of "in-transit" inventory in alleged 1Q07 adjustments).) CW13 claims that "VeriFone included the inflated inventory in the Company's publicly reported results" and that "the restatement confirmed the problems documented in his report." (*Id.* ¶ 137.) What he does not say, however, is whether the restatement had anything to do with the "inflated inventory" that CW13 purported to find. Given that the restatement was principally based on errors that had not even been made until *after* CW13's work is alleged to have been completed, it is difficult to see how it could.

CW13 says nothing at all about Periolat's incorrect entries. He does not claim that he believed that those entries were in error when they were made or that they made VeriFone's financial statements materially false. He does not allege that he ever told anyone that he believed this to be the case at any relevant time. Even if he had, given that the problem that his report purported to describe was not addressed by the restatement, this report could not have contributed to the knowledge on the part of Defendants Bergeron or Zwarenstein that the later-restated results were incorrect. Given that VeriFone's restatement does not appear to have corroborated CW13's view as to the inventory "variance" existing in Q1 2007, the more likely explanation for the alleged rejection of his report is that his report was incorrect. CW13's allegations provide no basis for a strong inference of scienter.[8]

3. Even if Periolat's Scienter Were Adequately Pleaded, This is Not Attributable to any Other Defendant.

As noted above, one other way in which the SAC is different from the CC is the addition of Paul Periolat as a defendant. But even if Plaintiff had successfully alleged knowledge or deliberate recklessness with respect to Periolat (which as set forth above and in Mr. Periolat's separate motion, it has not), this would still not suffice to allege scienter against any other Defendant, including VeriFone, Periolat's former employer, because Periolat was not an officer. "A defendant corporation is deemed to have the requisite scienter for fraud only if the individual corporate officer making the statement has the requisite level of scienter." *In re Apple Computer, Inc., Sec. Litig.*, 243 F. Supp. 2d 1012, 1023 (N.D. Cal. 2002); *see also In re Int'l Rectifier Corp. Sec. Litig.*, No. CV 07-2544-JFW, 2008 WL 4555794, at *21) (C.D. Cal. May 23, 2008) ("For scienter to be attributed to International Rectifier, Plaintiffs must sufficiently plead that at least one of International Rectifier's officers had the requisite scienter at the time they made the allegedly misleading statements"). Periolat, a non-officer, is not alleged to have made any of the public statements that Plaintiff challenges as false or misleading. Because Plaintiff fails to show that any Defendant who did make statements possessed scienter, neither the individual

[8] Plaintiff also alleges that VeriFone's SEC filings and press releases somehow support an inference of scienter in their discussion of inventory valuation and inventory figures. (*See* SAC ¶¶ 140-45.) As discussed, Plaintiff fails elsewhere in the SAC to allege specific facts indicating that any Defendant knew that Periolat had made erroneous inventory entries at the time that VeriFone made these filings and statements. Plaintiff alleges no particular fact indicating any such knowledge in this section of the SAC, either. Thus, there is no basis for inferring scienter based on these inventory-related comments in Company filings.

Defendants nor VeriFone can be liable for securities fraud. *See Glazer*, 549 F.3d at 745 (holding that "the PSLRA requires [plaintiff] to plead scienter with respect to those individuals who actually made the false statements"); *Nordstrom* v. *Chubb*, 54 F.3d 1424, 1435-36 (9th Cir. 1995) (rejecting plaintiff's "collective scienter" theory).

C. Plaintiff Has Failed to Cure the Deficiencies of the Consolidated Complaint

Plaintiff's new allegations do not plead scienter adequately. The allegations lifted (and, in some respects, repackaged) from Plaintiff's Consolidated Complaint do not either.

1. Defendants' Stock Trades Still Do Not Raise a Strong Inference of Scienter[9]

When granting Plaintiff leave to amend the Consolidated Complaint, the Court identified Defendants' stock sales as an area where Plaintiff's allegations might improve and provided specific suggestions for how that might be done. Tellingly, Plaintiff has not taken up the Court's suggestion.

Stock sales by corporate insiders "may constitute circumstantial evidence of scienter . . . only when such sales are 'dramatically out of line with prior trading practices at times calculated to maximize the personal benefit from undisclosed inside information.'" (Order at 9 (quoting *Metzler*, 540 F.3d at 1066-67).) "Three factors are relevant to this inquiry: (1) the amount and percentage of the shares sold; (2) the timing of the sales; and (3) whether the sales were consistent with the insider's trading history." (Order at 9 (citing *Metzler*, 540 F.3d at 1067).) These factors, which are discussed below, weigh heavily against the required strong inference of scienter.

Certain other factors undermine Plaintiff's attempt to plead scienter even more. First, because "insufficient allegations of fraud elsewhere in the complaint have a spillover effect" on insider stock sale allegations, *In re Vantive Corp. Sec. Litig.*, 283 F.3d 1079, 1093 (9th Cir. 2002), Plaintiff's failure to allege particularized facts demonstrating Defendants' knowledge as to incorrect financial statements necessarily weakens any inferences that can be drawn from stock trading. Second, nearly all of the sales of personal stock made by VeriFone insiders during this period were made pursuant to non discretionary 10b5-1 plans, further negating an allegation of suspiciousness.[10] *See Metzler*, 540 F.3d at

[9] This brief only addresses stock trade allegations concerning Atkinson, Bergeron, and Bondy.

[10] While Plaintiff insists that Defendant Atkinson amended his 10b5-1 trading plan during the Class Period, he is alleged to have done so in January 2007, *prior* to the first of Periolat's alleged

1067 n.11 (stating that "[s]ales according to pre-determined plans may 'rebut [ ] an inference of scienter'") (citing *In re Worlds of Wonder Sec. Litig.*, 35 F.3d 1407, 1427-28 (9th Cir. 1994)). Third, Paul Periolat, the person who is alleged to have made the erroneous accounting entries (and to have done so knowingly, according to Plaintiff), is not alleged to have sold a single share of VeriFone stock. Accordingly, Plaintiff attempts to portray a fraudulent scheme, the purpose of which was to enrich the wrongdoers, in which the person alleged to be the principal wrongdoer is not alleged to have benefited by so much as a dollar.

a. The Amount of Defendants' Stock Trades Was Not Unusual

This Court has already rejected the type of stock trading data that Plaintiff again presents in the SAC. In its prior order, the Court held that Plaintiff's allegations of stock trading for Zwarenstein and Atkinson – which were divided in Plaintiff's opposition to Defendants' and Zwarenstein's motions to dismiss into simplistic "before the Class Period" and "during the Class Period" time periods – was "inadequate to meet the requirement of providing a 'meaningful trading history for purposes of comparison,'" and therefore insufficient to create an inference of scienter. (Order at 10 (quoting *Digimarc*, 552 F.3d at 1005).) Undeterred, Plaintiff alleges that simply listing Defendants' stock sales and dividing them up into broad "before the Class Period" and "during the Class Period" data provides for a strong inference of scienter. (*See* SAC ¶¶ 199-215 & Ex. 4.) As this Court has already determined, this data "does little to provide context" for Defendants' trading, and cannot support an inference of scienter. (Order at 10.)

(i) Bergeron and Bondy/GTCR

Even if this type of crude before/during analysis could support an inference of scienter, the new allegations in the SAC actually *rebut* any inference that the amount of stock sold by Bergeron and GTCR was suspicious. According to the SAC itself, Bergeron sold more shares before the Class Period (2,584,870) than during the Class Period (2,466,335), and Bondy's employer, GTCR, sold nearly

accounting errors and the subsequent erroneous earnings reports. (*See* SAC ¶¶ 13, 210.) In any event, as discussed below, Plaintiff presents no allegations supporting any inference that Atkinson possessed material nonpublic information about VeriFone's inaccurate financials at any time, let alone at the time he amended his 10b5-1 plan. Plaintiff does not allege that Defendant Bergeron modified his 10b5-1 trading plan during the Class Period. (*See* SAC at ¶¶ 201-03.) Defendant Bondy made no sales of personal Verifone stock.

twice as many shares before the Class Period (18,896,399) as during the Class Period (9,800,000). (SAC ¶ 200.) Similarly, the value of the stock that GTCR and Bergeron allegedly sold during the Class Period was in line with pre-Class Period amounts – GTCR allegedly sold $350 million in shares before the Class Period, and $359 million in shares during the class period; Bergeron allegedly sold $60 million in shares before the Class Period, and $92 million in shares during the Class Period. (*Id.*) Simply put, Plaintiff's allegations reveal that Bergeron and GTCR's trading amounts were not "'dramatically out of line with prior trading practices.'" (Order at 9 (quoting *Metzler*, 540 F.3d at 1066-67).) The amount of stock that Bergeron and GTCR retained *after* the allegedly fraudulent sales further rebuts an inference of scienter. Both Bergeron and GTCR held on to enough stock after the challenged sales (over 11 million shares worth in excess of $400 million) to incur enormous losses – losses that negate any inference that either of them "pumped" the price of VeriFone's stock in order to profitably "dump" their holdings. (*See* D.E. 164 at 16-17.)

(ii) Atkinson

Plaintiff similarly fails to allege facts demonstrating that Defendant Atkinson's stock sales were of an unusual amount. In the Pre-Class Period, Atkinson is alleged to have sold approximately 91,000 shares. (SAC ¶ 200.) This is roughly half of – and in line with – the 181,000 that he is alleged to have sold during the Class Period. (*Id.*); *cf. Vantive*, 283 F.3d at 1095 (holding that insider's sales during class period were not "dramatically out of line" with prior trading practices where she had sold 10,000 shares prior to class period, and sold 61,000 shares during period). This conclusion is still more obvious when the Class Period sales are reduced by the 35,000 shares that Atkinson allegedly sold *after he left VeriFone*. (*See* SAC ¶ 28; SAC Ex. 4.)[11]

[11] As in the CC, Atkinson is treated as an afterthought in the SAC. Plaintiff's lone allegation as to Atkinson's mental state is that, "[a]s a senior officer at the Company who made misleading statements regarding the Lipman merger and received extra bonuses and stock awards for his participation in the merger, a strong inference arises that Atkinson was aware of VeriFone's internal control problems and its grossly distorted gross margin and EPS results." (SAC ¶ 211; see also CC ¶¶ 142, 155-56.) Plaintiff's allegation that Atkinson made a single false statement provides no facts supporting its assertion that Atkinson would have known the statement to be misleading – assuming that Atkinson's alleged statement that the post-merger company "will begin Day 1, completely integrated. [We] are locked and loaded," (SAC ¶¶ 28, 194, 208), can even appropriately be considered a statement of fact capable of being misleading. *See Brodsky* v. *Yahoo! Inc.*, 630 F. Supp. 2d 1104, 1113 (N.D. Cal. 2009) (finding "general optimistic statements" such as defendant's claim that "'all the pieces are coming together'" to be non-actionable). Plaintiff provides no allegation whatsoever as to what inside

* * *

Defendants' Class Period sales are in-line with their Pre-Class Period sales. In the Pre-Class Period, Defendants allegedly sold 21.6 million shares for approximately $413 million, while in the Class Period, Defendants allegedly sold 12.7 million shares for approximately $465 million. (SAC ¶ 200.) The history of the amounts that Defendants traded at various times does not "actually support[] plaintiffs' assertions that the activity during the class period was 'dramatically out of line with prior trading practices.'" (Order at 16 (quoting *Metzler*, 540 F.3d at 1066-67).)

b. The Timing Of Sales and Trading History Were Not Unusual

"[S]tock sales are helpful only in demonstrating that certain statements were misleading and made with knowledge or deliberate recklessness when those sales are able to be related to the challenged statements." *Vantive*, 283 F.3d at 1093. Plaintiff has failed to remedy its previously rejected allegation that Defendants' stock sales were suspiciously timed. While Plaintiff now includes lists of alleged stock trades by Defendants as Exhibit 4 to the SAC, it makes no effort to link the specific trades on its lists to any alleged misstatement or guilty knowledge on the part of a single Defendant.

(i) Bergeron

At the outset, Bergeron's stock sales could not have been suspiciously timed because they were sold at non-discretionary times pursuant to his 10b5-1 plan. Plaintiff generally alleges that Bergeron's trading was somehow linked to Periolat's accounting adjustments and Bergeron's alleged e-mail request to "fix the problem," (SAC ¶ 201), but a glance at Plaintiff's own trade-by-trade summary for Bergeron belies Plaintiff's assertion. Bergeron's alleged e-mail in response to the first below-forecast internal reports, and Periolat's first erroneous accounting adjustment, both allegedly occurred in February 2007. (*See* SEC Compl. ¶¶ 13-21.) But by January 10, 2007 – the month *before* Bergeron's alleged email and five months into the Class Period – Bergeron had already allegedly sold more than 800,000 shares of his stock – nearly one third of all the stock he sold during the Class Period. (*See* SAC

information Atkinson could conceivably have had and traded on after he left VeriFone. This Court has already observed that allegations based on Defendants' positions or their compensation are inadequate evidence of scienter. (*See* Order at 12, 15.) Moreover, Atkinson's "senior position" was in marketing, not accounting or finance. (SAC ¶ 28.) The combination of Class Period stock trades that are in line with out-of-class-period trades and inadequate factual allegations as to Atkinson's knowledge of VeriFone's accounting leave no basis for any inference of scienter on Atkinson's part.

Ex. 4.) Bergeron then sold 1.64 million shares at regular intervals over the next ten months – Plaintiff does not point to any particularly heavy trading at the time of the accounting entry or e-mail. (*Id.*) Plaintiff's own itemized list makes clear that Bergeron sold shares at a slower overall rate in the fifteen class-period months after Periolat's erroneous accounting entries than before, refuting the bald assertion that Bergeron's sales were linked to any alleged misstatements in VeriFone's financial statements.

(ii) Bondy/GTCR

Similarly, a glance at the itemized trading history that Plaintiff alleges for GTCR reveals a consistent trading pattern from December 2005 through September 2007. (*See id.* (showing 2.5 million shares sold on 12/27/2005; 3 million shares sold on 6/23/2006; 3 million shares sold on 12/19/2006; 3.5 million shares sold on 6/25/2007; and 3.3 million shares sold on 9/13/2007).) Plaintiff's failure even to mention these itemized trades makes clear that there is no inference to be drawn from them that is useful to Plaintiff.[12]

(iii) Atkinson

In the case of Atkinson, Plaintiff's trading history allegations fare no better. While Plaintiff sets out some of Atkinson's Pre-Class Period and Class Period trading history, it fails to tie any of Atkinson's alleged specific sales to any alleged misleading statements or guilty knowledge on Atkinson's part. (*See* SAC ¶ 210); *see Vantive*, 283 F.3d at 1093. As discussed above, Plaintiff fails to allege any facts demonstrating that Atkinson, a marketing executive, possessed, or could reasonably be expected to have possessed, non-public information about VeriFone's inventory accounting or financial reporting systems. Atkinson's trading history thus provides no evidence of scienter.

2. VeriFone's Restatement Still Does Not Raise a Strong Inference of Scienter

Plaintiff repeats its allegation that the mere fact of VeriFone's restatement provides a strong inference of scienter. (*Compare* SAC ¶¶ 114, 116-25 *with* CC ¶¶ 77-78, 81-89.) As this Court

[12] Other than the allegations about GTCR's trades, Bondy and GTCR get even shorter shrift in the SAC than does Atkinson. Plaintiff fails to allege any facts demonstrating that Bondy or GTCR made statements that would connect GTCR's alleged stock sales to purportedly fraudulent conduct. And the only facts that Plaintiff alleges to suggest possession of non-public information is the amount of stock that GTCR sold during the Class Period and Bondy's presence on VeriFone Board Committees. (SAC ¶¶ 213-15.) But the extent of GTCR's holdings and its consistent sales pattern provide no basis to infer scienter. And Plaintiff's allegations about Bondy's role at VeriFone provide absolutely no basis for any inference of scienter. (*See id.* ¶ 215.)

previously noted, however, "the necessity of a restatement is not enough, standing alone, to create a strong inference of scienter." (Order at 11 (quoting *Digimarc*, 552 F.3d at 1000).) *Digimarc* makes clear that Plaintiff has not satisfied the first exception to this rule, under which a false statement is indicative of scienter where "allegations regarding a manager's role in that company . . . are particular and suggest that defendant had actual access to the disputed information." (Order at 11 (citing *Digimarc*, 552 F.3d at 1000).) In *Digimarc*, allegations that management "closely reviewed . . . accounting numbers," and "that top executives had several meetings in which they discussed quarterly inventory numbers" were "not enough to satisfy the narrow exception." 552 F.3d at 1000. The Ninth Circuit explained that allegations of management access to purportedly manipulated data "d[id] not support the inference that management was in a position to know that such data was being manipulated." *Id*. at 1000-01. As noted above, the SEC Complaint simply alleges that management was "aware of [Periolat's] adjustments." (SEC Compl. ¶ 27; *see* SAC ¶ 115.) Just as in *Digimarc*, management's alleged awareness of Periolat's inventory adjustments does not support an inference that management was aware that Periolat was wrong because there is no indication that management "had access to the underlying information from which the accounting numbers were derived." *Digimarc*, 552 F.3d at 1001.

As this Court recognized, the second exception to the general rule that the mere fact of a restatement is not sufficient to allege scienter is also inapposite here. (*See* Order at 11-12.) This exception "permits an inference of scienter where the information misrepresented is readily apparent to the defendant corporation's senior management," and "the defendants' awareness of the information's falsity can be assumed" because the falsity "was obvious from the operations of the company." *Digimarc*, 552 F.3d at 1001 (citing *Berson* v. *Applied Signal Tech., Inc.*, 527 F.3d 982, 987-89 (9th Cir. 2008)). The SAC contains no new allegations demonstrating why the technical inventory accounting errors that led to the restatement were "obvious" to management. Rather, the SAC's description of the technical errors involving inventory calculations, (*see, e.g.*, SAC ¶¶ 119-24), combined with the facts that 1Q07-3Q07 were the first reporting periods following the Lipman acquisition, (*see id.* ¶ 2) – and that the restatement errors are alleged to relate to Lipman inventory issues, (*see id.* ¶¶ 119-24) – negates such an inference. *See Digimarc*, 552 F.3d at 1001 (holding that falsity of technical and "definitional" accounting representations "would not be immediately obvious to corporate management"); *In re*

Cadence Design Sys., Inc., Sec. Litig., 654 F. Supp. 2d 1037, 1049 (N.D. Cal. 2009) (same).

3. Plaintiff's Other Recycled Allegations Still Do Not Raise a Strong Inference of Scienter

Other allegations from the previously-rejected Consolidated Complaint that make encore appearances in the SAC still fail to plead scienter.

Plaintiff again relies on allegations from Confidential Witnesses 1-10. (*Compare* SAC ¶¶ 157-70, 172-83 *with* CC ¶¶ 91-104, 106-17.) The variety of shortcomings discussed in the previous round of briefing still apply to the allegations of CWs 1-10, which are largely unchanged in the SAC. As this Court noted, the allegations by the ten CWs simply do not support an inference that Defendants knew about Periolat's allegedly incorrect journal entries, much less that Defendants intended the incorrect entries or were deliberately reckless as to the errors. (Order at 13.)

Plaintiff's continued reliance on Zwarenstein and Bergeron's statements made in connection with boilerplate statements in the "Controls and Procedures" section of VeriFone's SEC filings, (SAC ¶ 145, 155, 189), provides no support for an inference of scienter. (Order at 12-13); *see Digimarc*, 552 F.3d at 1003-04 (rejecting plaintiff's reliance on boilerplate language from "controls and procedures" section of defendant's 10-Q).[13]

Zwarenstein's resignation from VeriFone and Periolat's termination also do not provide evidence of scienter. (*Compare* SAC ¶ 185 *with* CC ¶¶ 119-20.) As this Court concluded last time, "[t]he most reasonable inference, absent other support, is that personnel changes occurred because of the mistake and real or perceived underlying negligence." (Order at 14); *see also Digimarc*, 552 F.3d at 1002. Plaintiff has provided no particular allegations indicating that Periolat left VeriFone because of fraud, rather than because of his inventory accounting errors.

Plaintiff's allegations that Defendants' incentive compensation provides evidence of scienter also founder once more. (*Compare* SAC ¶¶ 216-228 *with* CC ¶¶ 145-156.) As the Court

[13] Plaintiff's allegations that Defendants' forward-looking statements and predictions from 2006 and 2007 are indicative of scienter, rejected previously, are no more persuasive now. (*Compare* SAC ¶¶ 154, 191-196 *with* CC ¶¶ 224-25, 157-61; Order at 14.) Plaintiff's inexplicable reliance on Defendants' 2008 restatement-related public statements and filings as evidence of scienter, (*compare* SAC ¶¶ 186-88 *with* CC ¶¶ 121, 123, 125), also fails again. These statements merely identify shortcomings in historical accounting controls that led to the restatement and provide no evidence of scienter. (*See* Order at 14-15.)

previously noted, in comparison to their alleged stock sales, Defendants' incentive bonuses were relatively modest. (Order at 15; *see* SAC ¶¶ 217-18, 222-24, 227.)

Finally, Plaintiff repeats its assertion that Lipman's pre-merger margins and sales data provides compelling evidence of scienter. (*Compare* SAC ¶¶ 147-52 *with* Pl.'s Opp. at 13-14; *see also* CC ¶¶ 56-57, 65-67, 73.) As detailed in Defendants' Reply Brief on the previous motion to dismiss, there were several reasons – known at the time, accepted by analysts, and referenced in the CC – why it was reasonable to believe the merged entity's gross margins could increase, even if Lipman's pre-merger margins were lower than VeriFone's, as a result of the acquisition. (*See* D.E. 182 at 5-6.)

D. The Totality of Plaintiff's Allegations Do Not Raise a Strong Inference of Scienter

As detailed above – and, as to many of the allegations, in this Court's order dismissing Plaintiff's prior complaint – not one of Plaintiff's SAC allegations establishes the required strong inference of scienter. The allegations taken together do not do so either. If anything, the non-fraudulent circumstances described in the SEC Complaint, combined with the non-suspicious stock trades (including the total lack of alleged trading by Periolat) and Plaintiff's continuing inability to locate a single confidential witness willing to allege that Periolat's entries were known by anyone at VeriFone to have been false when made, renders an inference (much less a strong inference) of fraud totally implausible. As was true of Plaintiff's prior complaint, "[t]here are many allegations in this case, but they fare no better when read in combination than when read independently." (Order at 15.)

II. PLAINTIFF FAILS TO STATE A CLAIM UNDER SECTION 10(b) AND SEC RULE 10b-5 OR UNDER SECTION 20A FOR INSIDER TRADING AGAINST DEFENDANTS

Plaintiff again alleges "suspicious" insider trading activity on the part of Defendants as a primary violation under Sections 10(b) and 20A and SEC Rule 10b-5. (SAC ¶¶ 199-215, 284.) Plaintiff's allegations do not support these claims. An insider trading claim, as with any alleged violation of Section 10(b), requires an allegation of scienter. *See Lipton* v. *Pathogenesis Corp.*, 284 F.3d 1027, 1035 n.15 (9th Cir. 2002). Because, as demonstrated above, Plaintiff has failed adequately to plead any allegations of scienter, the insider trading claims under Section 10(b) fail.

Similarly, "to prevail on their claims for violations of . . . § 20A, plaintiffs must first allege a violation of § 10(b) or Rule 10b-5." *Id.*; (*see* Order at 15). Plaintiff's Section 20A claim, thus,

fails. Plaintiff's Section 20A claim also fails because Plaintiff pleads no facts with specificity showing that any of Defendants possessed material, non-public information when they traded. *See Neubronner* v. *Milken*, 6 F.3d 666, 672 (9th Cir. 1993) (noting that plaintiffs must allege "specifically what information [defendant] obtained, when and from whom he obtained it, and how he used it for his own advantage"). Finally, Plaintiff's Section 20A claim again fails because the SAC does not adequately plead contemporaneous trades. *See id.* at 670. The purchases alleged by Plaintiff occurred days before or after the sales by Defendants and, thus, are not contemporaneous. (*See, e.g.*, SAC ¶¶ 287(a), (b), (d), (e), (f), (g) (Bergeron); 288(h) (Bondy)).[14] Courts are increasingly adopting a same-day trading requirement because, in an active market, one who did not trade on the same day as the insider could not have traded with the insider. *In re ASTResearch Sec. Litig.*, 887 F. Supp. 231, 233-34 (C.D. Cal. 1995) ("The same day standard is the only reasonable standard given the way the stock market functions"); *In re Countrywide Fin. Corp. Sec. Litig.*, 588 F. Supp. 2d 1132, 1204 (C.D. Cal. 2008) (noting that, on a motion to dismiss, the same-day rule is "a judicially manageable rule that balances market realities with a strong deterrent effect" and adopting a same-day-or-the-day-after definition of "contemporaneous.").

III. PLAINTIFF FAILS TO STATE A CLAIM UNDER SECTION 20(a) FOR CONTROL PERSON LIABILITY AGAINST ANY DEFENDANT

Plaintiff has likewise failed to state a claim under Section 20(a) of the Exchange Act. To establish "control person" liability under Section 20(a), a plaintiff must first allege (1) a primary violation and (2) that the defendant exercised actual control over the primary violator. *Digimarc*, 552 F.3d at 990. Because Plaintiff has failed adequately to plead a primary violation as to any Defendant, its Section 20(a) claim against Defendants should also be dismissed. (Order at 15.)

Plaintiff has also again failed to plead that Defendants possessed or exercised the "'significant degree of day-to-day operational control'" required for liability under Section 20(a). *In re McKesson HBOC, Inc. Sec. Litig.*, 126 F. Supp. 2d 1248, 1277 (N.D. Cal. 2000) (citation omitted).

[14] The only "same-day" trade alleged with respect to Bergeron is on December 1, 2006, at least two months before Periolat's alleged accounting errors. (*See* SAC ¶ 287(c).) The only remotely contemporaneous trades with respect to Bondy are purchases *eight* and *ten* days after GTCR sold VeriFone stock. (*See id.* ¶ 288(h).) And, while a number of the alleged trades against Defendant Atkinson are similarly defective, (*see, e.g., id.* ¶¶ 288(a), (c), (f)), the failure to allege any basis for believing that Atkinson traded on material, non-public information is, itself, fatal to Plaintiff's claim.

Plaintiff has alleged no facts of control with respect to Atkinson and Bondy aside from Atkinson's position as an executive vice president and Bondy's role as a director who served on one committee. (*See* SAC ¶¶ 295-96.) Generic boilerplate allegations are insufficient to state a claim for control person liability. *See In re Hansen Natural Corp. Sec. Litig.*, 527 F. Supp. 2d 1142, 1163 (C.D. Cal. 2007). As to Bergeron, Plaintiff has not alleged facts showing that he had operational control over Periolat, or even communicated directly with Periolat. Instead, Plaintiff relies on allegations regarding Bergeron's high-level position and general awareness of VeriFone's operations, but nowhere alleges that Bergeron – who is not alleged to have any kind of accounting background – directed Periolat or had any contact with him at all. Plaintiff's allegations simply are not sufficient. *See id.* But even if Bergeron did "control" Periolat, Plaintiff has not alleged facts showing that Periolat committed a primary violation.

IV. THE SECOND AMENDED COMPLAINT SHOULD BE DISMISSED WITH PREJUDICE

Courts consider five factors in deciding whether to grant leave to amend: "(1) bad faith; (2) undue delay; (3) prejudice to the opposing party; (4) futility of amendment; and (5) whether the plaintiffs have previously amended their pleading." (Order at 16.) "Futility alone can justify the denial of a motion for leave to amend." (*Id.*) Here, futility and the previous failed amendment strongly counsel against granting further leave to amend. The Court specifically gave leave to amend the first time to permit Plaintiff to plead scienter based on stock trading history, asking for "detailed and comprehensive comparisons of trades stretching over the course of a number of years." (*Id.*) Plaintiff has failed to make these allegations, undoubtedly because the stock trading history simply does not support an inference of scienter. Plaintiff also bases the bulk of the new allegations in the SAC on an SEC Complaint that actually undermines its case for scienter by providing a far more plausible and cogent non-fraud alternative. The remainder of Plaintiff's allegations is simply a rehash of claims this Court has already rejected. This is now Plaintiff's third attempt (consolidated, first amended and second amended complaints). That Plaintiff has "failed to correct the[] deficiencies in the [SAC] is 'a strong indication that [it] ha[s] no additional facts left to plead.'" *Digimarc*, 552 F.3d at 1007 (quoting *Vantive*, 283 F.3d at 1098). Accordingly, this Court should dismiss the SAC with prejudice.

Date: March 5, 2010

/s/ Brendan P. Cullen
Brendan P. Cullen (SBN 194057)

Scott C. Hall (SBN 232492)
Sverker K. Hogberg (SBN 244640)
Achyut J. Phadke (SBN 261567
SULLIVAN & CROMWELL LLP
1870 Embarcadero Road
Palo Alto, California 94303
Telephone: (650) 461-5600
Facsimile: (650) 461-5700

Robert A. Sacks (SBN 150146)
SULLIVAN & CROMWELL LLP
1888 Century Park East
Los Angeles, California 90067
Telephone: (310) 712-6600
Facsimile: (310) 712-8800

Attorneys for Defendants VERIFONE HOLDINGS, INC., DOUGLAS G. BERGERON, WILLIAM G. ATKINSON and CRAIG A. BONDY